

June 1, 2015

Madame Mayor and City Council,

As part of our annual efforts, the Budget Advisory and Financial Planning Committee (the “Committee”) has completed a review of the most recent 7 year projections as provided by the City Finance Director. The revenue methodology is consistent with prior years, which has proven to be somewhat conservative given the strength of the real estate market and local economy. Overall, we felt the assumptions used, and the results presented, to be reasonable and prudent, subject to a few comments noted below. As in prior years, the projections continue to show that the long term financial health of the City is dependent on the continuation of the Municipal Services Parcel Tax.

The projections show a stable General Fund balance over the projection period, despite the City loaning \$800,000 to the Sewer Fund last year to initiate the next phase of sewer replacement. The Committee supports setting aside surplus funds in good times to sustain capital maintenance projects over the long term. Although the General Fund balance looks healthy over the planning period, it is important to note that (1) certain costs of current services (specifically pension and retiree healthcare costs and facility maintenance) are being deferred and would turn surpluses into deficits if fully funded, (2) no monies are being reserved for large scale capital projects such as the aquatics facilities and parks and recreation facilities, and (3) the projections assume no economic downturn. The real estate cycle is now 4-5 years in recovery and it has been 8 years since the last peak.

The Committee feels the objective of long term financial planning for the City is to take steps to ensure that current services are being paid for in the current year to the extent possible and funds for future requirements (retirement commitments and facilities maintenance) are being set aside on a current basis – especially in good economic times. The City has made significant strides in funding facilities maintenance and equipment replacement reserves over the past few years, and the projections continue that trend. The City has recently completed a five year plan for facility maintenance based on immediate priorities developed with department heads, but the City still lacks a basic long term vision of facility maintenance which would better guide annual funding to make sure the City is on a long term sustainable path. We recommend that this committee undertake at least a rudimentary attempt at putting together the longer term facility maintenance vision as part of examining the Municipal Services Parcel Tax later this year.

As with last year, it should be noted that although some money is being put aside into the OPEB every year, the amount is far less than the accruing liability for

current services – by as much as \$600,000 per year. This shortfall acts like an implicit loan and the City will have to make up the shortfall in the future. Fortunately the City can demonstrate future resources in the form of excess funding of the Piedmont Police and Fire Pension Fund as well as budget funds currently being applied to Side Fund debt service which will be available in 5 years (once the Side Fund loan is repaid). We also recommend that this Committee further examine the viability of the OPEB in the future given these resources.

Finally, there are many assumptions around pension benefits that require caution.

1. CalPERS has provided longer term estimates for employer pension contributions that rise to 50% of salary for safety employees. The Committee has several times warned of large increases coming (and these may not be the last). The City currently has a sharing arrangement with employees whereby they pick up approximately 50% of the pension cost above certain thresholds (which are currently being exceeded).
2. On the other hand, the projections assume no change to the mix or Tier I vs Tier II and II employees. That assumption seems conservative as it is likely that Piedmont will experience material employee turnover in the coming years which will likely result in lower real employer pension costs.

The Committee appreciates the opportunity to present our findings and look forward to continuing more in depth work on the Municipal Services Parcel Tax in the Fall. Please let us know if you have any questions or would like any additional analysis.

Thank you,

Bill Hosler

Chair of the Budget Advisory and Financial Planning Committee